



Minnesota

Department of Finance

April 2002

State Revenues on Forecast in February and March

Net general fund revenues totaled \$1.834 billion during February and March, \$10.4 million (0.6 percent) more than forecast. Receipts from the four major taxes were \$1.565 billion, \$12.6 million (0.8 percent) less than forecast, while other tax and non-tax revenues were \$23 million (9.3 percent) above projections.

Summary of Tax Receipts: February – March 2002

	<u>Estimate</u>	<u>Actual</u>	<u>Variance</u>	<u>Percent</u>
	----- (\$ in millions) -----			
Income	821.6	810.1	(11.5)	(1.4)
Sales	541.0	542.8	1.8	0.3
Corporate	156.0	156.9	0.9	0.6
Motor Vehicles	58.8	55.0	(3.8)	(6.5)
Other	<u>246.6</u>	<u>269.6</u>	<u>23.0</u>	<u>9.3</u>
Total	1824.0	1834.4	10.4	0.6

There is evidence that the U.S. economy strengthened during the first quarter of 2002, **but state tax collections offer no reason to believe that Minnesota's revenue forecast was too pessimistic.** Individual withholding tax collections and gross sales tax receipts, the two revenue sources tied most closely to the current performance of the economy, were both below forecast. (see page 4) Motor vehicle sales tax collections were also below projections. The weakness in receipts is further demonstrated by the fact that both withholding tax receipts and gross sales tax collections are less than year-earlier levels. Without strong growth in deed and mortgage tax receipts (up \$14 million from forecast and more than 80 percent from last year's level), and stronger than anticipated growth in departmental earnings and regional treatment center collections, state revenues during the past two months would have been below forecast.

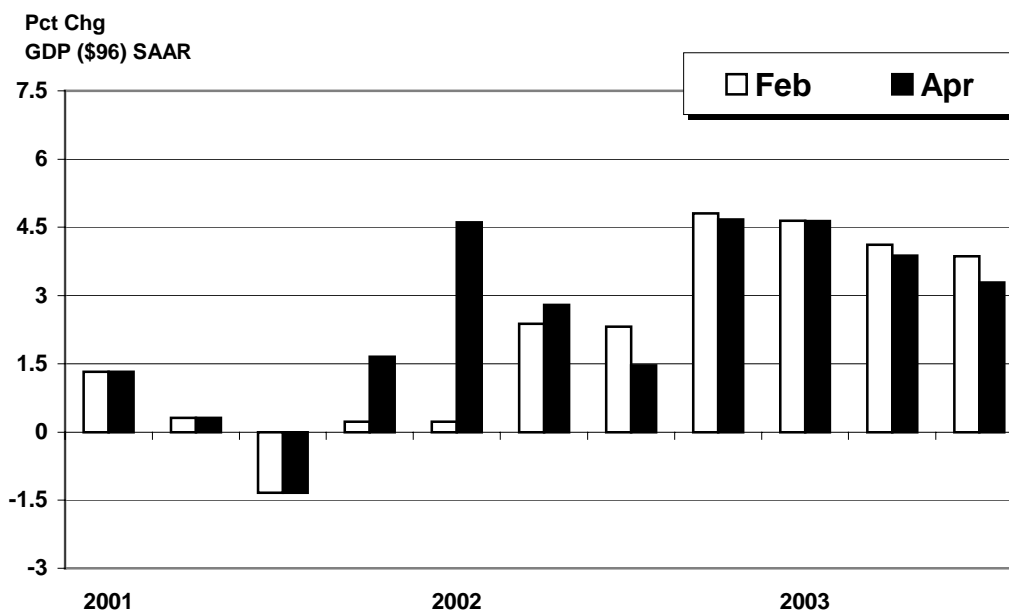
Individual income tax receipts include only withholding and individual estimated tax payments. As always, variances in refunds and final payments are not reported during the tax processing season. Variations in the rate of processing and filing make it impossible to make realistic projections of refunds paid and final payments received through March 31. Variances for individual income tax refunds and final payments for tax year 2001 will be reported as part of the July *Economic Update*.

Very Strong Real GDP Growth Is Now Expected for First Quarter 2002

The mini-recession of 2001 is over and all signs now point to a real GDP growth rate of 4.0 percent, or more for the first quarter of 2002. The enormous inventory liquidation, which began in early 2001, appears to be ending, consumer confidence is strong, payroll employment appears to be growing, and manufacturing orders are up. The U.S. Department of Commerce also now reports that real GDP grew at a 1.7 percent rate during the fourth quarter, up 1.5 percentage points from their initial reading at the end of January.

Like every other forecaster DRI-WEFA, Minnesota's national economic consultant, has revised its outlook significantly since the first of the year, raising projected growth rates for the fourth quarter of 2001 and the first quarter of 2002 substantially. The quicker-than-hoped-for end to the inventory draw down has been particularly important in the improved outlook for the first quarter. But, as the chart below indicates, there has been little change in the outlook for the remaining quarters of this biennium. All that has happened is that inventory drawdown stopped more abruptly than anticipated.

DRI Believes Economy Grew at a 4.6 Percent Annual Rate During First Quarter 2002

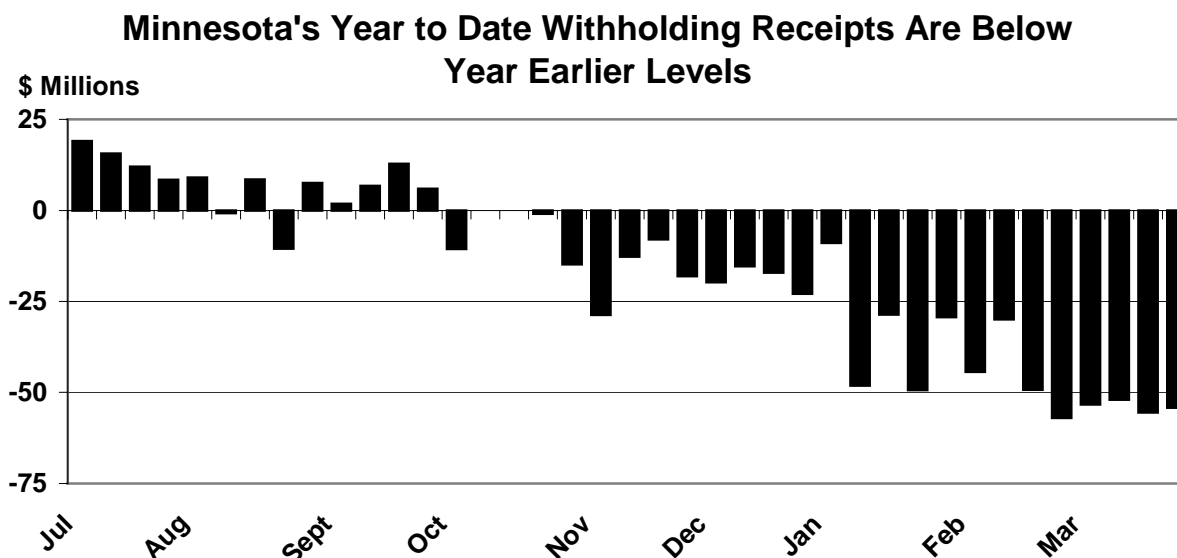


One strong quarter will not fully resolve all the problems facing the U.S. economy, however. Further inventory improvement will help boost second quarter growth as well, but after that, DRI notes the outlook “depends on a revival of business investment and sustained increases in consumer spending.” DRI now expects a real GDP growth rate of 2.3 percent for 2002, up 1.3 percentage points from February's estimate of 1.0 percent. The Blue Chip Consensus now calls for a real growth rate of 2.6 percent.

Clearly international events could adversely affect the outlook. DRI assigns a 25 percent probability to a double-dip recession (up 5 percent from February), but a 20 percent probability to a stronger than forecast recovery. The probability assigned to their baseline forecast is 55 percent.

Good National Economic News Has Not Been Reflected in State Revenues

To this point Minnesota tax revenues do not appear to have benefited from the improving national economy. Fourth quarter revenues were weaker than forecast, and revising the national economic growth rate will not increase the amount already collected. Similarly, even though the annualized first quarter 2002 real GDP growth rate is now expected to be about 4 percentage points higher than was assumed for February's revenue forecast, state revenues for the last two months were only \$10 million (0.6 percent) above forecast, and withholding tax receipts were \$10 million below forecast. Surprisingly, withholding tax receipts have been below year earlier levels since last fall, and the gap between current and year earlier levels has been widening. Gross sales tax receipts are also below year earlier levels.



Finance Department economists note that the unusual divergence between growth rates for the national economic aggregates and state withholding and sales tax receipts means that neither the change in real GDP, nor the change in the real GDP growth rate, is for the short term at least, a reliable guide for anticipating the effect of a change in the economic outlook on the state revenue forecast. State revenue growth has always lagged an upturn in the economy, and the increased importance of performance-based compensation appears to have accentuated that trend in this recovery.

Comparison of Actual and Estimated Non-Restricted Revenues

(\$ in thousands)

	March Year-to-Date			March & February 2002		
	Forecast Revenues	Actual Revenues	Variance Act-Fcst	Forecast Revenues	Actual Revenues	Variance Act-Fcst
Four Major Revenues:						
Individual Income Tax						
Withholding	3,603,920	3,593,848	-10,072	771,000	760,928	-10,072
Declarations	612,967	611,550	-1,417	50,600	49,183	-1,417
Miscellaneous	99,618	99,618	0	0	0	0
Gross	4,316,506	4,305,016	-11,490	821,600	810,110	-11,490
Refund	88,291	88,291	0	0	0	0
Net	4,228,215	4,216,725	-11,490	821,600	810,110	-11,490
Corporate & Bank Excise						
Declarations	457,180	455,558	-1,621	153,400	151,779	-1,621
Miscellaneous	94,553	108,952	14,399	25,600	39,999	14,399
Gross	551,733	564,511	12,778	179,000	191,778	12,778
Refund	122,041	133,893	11,853	23,000	34,853	11,853
Net	429,692	430,617	925	156,000	156,925	925
Sales Tax						
Gross	2,870,719	2,869,761	-958	589,160	588,202	-958
Refunds	195,159	192,344	-2,815	48,178	45,363	-2,815
Net	2,675,560	2,677,417	1,857	540,982	542,839	1,857
Motor Vehicle Sales						
	313,863	310,037	-3,826	58,838	55,012	-3,826
Other Revenues:						
Inherit/Gift/Estate	51,392	53,395	2,003	9,400	11,403	2,003
Liquor/Wine/Beer	43,660	42,026	-1,634	10,615	8,981	-1,634
Cigarette & Tobacco/Cont Sub	125,187	125,719	533	27,462	27,995	533
Deed and Mortgage	156,877	170,889	14,012	25,031	39,043	14,012
Insurance Gross Earnings	133,061	125,925	-7,136	74,900	67,764	-7,136
Lawful Gambling	38,093	38,323	230	8,390	8,620	230
Health Care Surcharge	93,663	93,342	-321	21,348	21,027	-321
Other Taxes	922	915	-7	271	264	-7
DHS RTC Collections	50,027	57,483	7,456	6,930	14,386	7,456
Income Tax Reciprocity	47,899	47,899	0	0	0	0
Investment Income	60,997	64,885	3,888	7,001	10,889	3,888
Tobacco Settlement	147,734	147,734	0	0	0	0
Departmental Earnings	145,073	150,749	5,676	23,298	28,974	5,676
Lottery Revenues	23,484	24,547	1,063	4,280	5,343	1,063
2000 Sales Tax Rebates	-32	-32	0	0	0	0
2001 Sales Tax Rebates	7,498	6,552	-947	251	-696	-947
Revenues yet to be Allocated	5,758	2,466	-3,292	-3,838	-7,130	-3,292
Residual Revenues Less Refunds	77,432	78,300	868	36,041	36,909	868
Other Subtotal	1,208,724	1,231,117	22,393	251,380	273,772	22,393
Other Refunds	13,358	12,766	-592	4,843	4,251	-592
Other Net	1,195,366	1,218,351	22,985	246,537	269,522	22,985
Total Gross						
	9,261,545	9,280,442	18,896	1,899,978	1,918,874	18,896
Total Refunds						
	418,849	427,294	8,445	76,021	84,466	8,445
Total Net						
	8,842,697	8,853,148	10,451	1,823,957	1,834,408	10,451